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DEFENSE EQUIPMENT

Zofia Sobiepanek

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SUMMARY

The sweeping economic and political changes that have transformed Poland since the collapse of communism in 1989 have had significant effects on the Polish defense sector. With its entry into NATO, Poland's enemies of forty years are now its allies. From the ashes of a centrally planned economy a vibrant free-market economy has emerged. The defense industry has had to change its client base and reorganize itself. Of the eight governments that have held power during the last twelve years, it is the current Government of Poland (GOP) that has shown the most serious commitment to reorganizing and privatizing the defense industry.

Since 1994, Poland has been among the fastest growing economies in Europe. Poland's gross domestic product (GDP) grew by 4.1% in 2000, a relatively strong performance in the context of Europe. The Polish government projects GDP growth of around 4.5% for 2001. Poland's current account deficit dropped in 2000, reaching a level of 6.2% of GDP, versus 7.5% in 1999. Total available funds for the Ministry of Defense (MOD) for 2001 amount to 15.4 billion PLN (about USD 4 billion), which constitutes 1.97% of GDP. This amount represents a 2% growth in comparison with 2000 budget allocations. According to the Central Statistics Office (GUS), in the period of January to November 2000 exports increased by more than 15% (amounting to USD 28.8 billion) above the same period in 1999. Imports grew by 7.4%, totaling USD 44.7 billion (about USD 700 million) lower than in 1999, making the trade deficit USD 15.9 billion. The average rate of inflation in consumer prices for 2000 was 9.8%, up from 7.3% in 1999. The government forecasts an average annual inflation rate of 6.8% for 2001. After a steady decline in the unemployment rate to 11.4% in January 1999, the figure went up to 13.6% in January 2000 and rose again to 15.6% in January 2001. This increase is partially due to a peak in the number of workers entering the workforce, increasing efficiency of the workforce and reductions in personnel at several large state owned entreprises.

Current forces of change in the military, the defense industry and the economy are expected to bring opportunities for foreign companies. A long-delayed reorganization and privatization plan is expected to materialize in 2001. Poland's membership in NATO has already brought opportunities for upgrades and adjustment in that area. Defense firms, still reeling from free market reforms, are seeking western partners. Opportunities for American firms exist mainly in investment, technology transfer, and co-production work. The latter is proving particularly important as the GOP weighs pending fighter aircraft and multi-role helicopter contracts. Receptivity to American companies is high due to a belief in the high quality of American products and friendly feelings toward the United States.

A. MARKET HIGHLIGHTS AND BEST PROSPECTS

I. MARKET PROFILE

Prior to 1989, the Polish defense industry benefited from many advantages. Companies manufacturing for the defense sector were given absolute priority in the acquisition of raw materials, technology and preferential credits. Also, they were exempt from paying taxes. Now faced with sharply reduced government subsidies, outdated technology and an under-employed work force, defense firms in Poland struggle to survive.

After 1989, three main factors negatively affected the long-term prospects for weapons production. The first was the collapse of the Warsaw Pact market, which accounted for 80-90 percent of defense sector output. The second was the advent of the new market economy. The third was the shrinking world arms markets, particularly for the generally low-technology weapons that were produced in Poland. In addition, the number of special orders written by the Ministry of Defense has been seriously reduced. According to current data, 80% of the present production of these companies is destined for civilian use and the remaining 20% goes to military applications. The total present output represents only 40% of the defense industry's military production capacity.

The Polish defense industry, however, still looks to the government for massive assistance. Successive government cabinets have billed defense industry restructuring as a key element of both industrial and national security policy. The current government struggled long to produce the new concrete privatization plan just accepted in January 2001. The defense industry believes that if its products are made compatible with NATO standards they could again become competitive, particularly if quality remains high and the price of the finished product remains low.

The following is a structure of 2001 MOD budget expenditures:

Saleries – 34.2%

Operating, maintenance and training costs – 30.9%

Pensions – 21.6%

Investment (armament, major equipment, R&D) – 11.6%

Other investments – 1.7%

II. BEST SALES PROSPECTS

Poland's shrinking defense industry is struggling for a place in the world defense market. Privatization has been a slow and painful process. The GOP is still struggling to develop. Several Polish plants have already entered into co-production ventures with foreign firms, including U.S. firms, for the production of defense articles, and could be expected to be open to similar arrangements with other U.S. firms after the privatization plan is implemented.

As mentioned above, no Polish manufacturers produce only defense articles. Plants manufacture a wide range of equipment, including aircraft engines and components, automotive/diesel engines and subassemblies, forging machines, air traffic control and navigation related equipment, electronics, tools, golf carts, appliances, agricultural equipment and wheel chairs. Many of these areas are also best prospects for the Polish market.

The CS Warsaw has identified the following defense-related industries as best prospects for the Polish market:

Aircraft and Parts
Telecommunications Equipment
Computer Software
Medical Equipment
Automotive Parts
Education and training
Food processing equipment
Pollution Control Equipment

B. COMPETITIVE ANALYSIS

I. DOMESTIC PRODUCTION

Before the changes of 1989, the defense sector consisted of 128 companies. Of those, 84 were reporting to the Ministry of Industry, 36 to the Ministry of Defense, and the rest to five other ministries. After 1989, 45 companies were designated by the government as being in the defense sector. Of these 45 companies, the GOP retains a controlling interest in 38 joint stock companies that are considered strategic companies in the interest of national security. Defense enterprises, the current subject of the defense reorganization and privatization plan, can be divided into the following branch groups:

Small arms, ammunitions and rifle factories
Electronic equipment
Armored equipment
Protective equipment
Aviation production
Chemical/engineering
Strategic sub-suppliers
R&D centers
Military repair enterprises
Trading companies (licensed for special trade)

The following is a listing of Poland's top ten defense companies:

Huta Stalowa in Stalowa Wola - armored vehicles

Bumar Labedy in Gliwice – armored vehicles

ZS Star in Starachowice – trucks

PZL-Rzeszow in Rzeszow - aircraft

PZL-Swidnik in Swidnik - aircraft

PZL-Mielec in Mielec - aircraft

FLK Krasnik in Krasnik- ammunition parts

ZTSz Gamrat in Jaslo- rocket fuel

ZM Mesko in Skarzysko-Kamienna - ammunition

Radwar in Warszawa - radar, command systems

The number of private companies cooperating with the defense sector is not officially known, but these firms play an important role as suppliers of military products. Currently, these companies supply the Polish army with cars, computers, clothing (including bulletproof vests), food products and printed materials. The number of members of the Polish Chamber of Defense Companies (Polska Izba na Rzecz Obronnosci Kraju) reflects the growing role of the private sector in supplying the Polish military. The Chamber, which was established in 1995, has almost 180 members. Half of its members are private firms.

Restructuring the Polish defense industry

Because of their precarious financial situation, Polish defense firms have shown little interest in importing foreign equipment. Between 1986 and1991, Poland exported 50% of its military production to the Soviet Union. Today, Poland exports only about 13% of its military production. The majority of defense exports include ammunition and spare parts. The largest importers of Polish military products are Yemen, India, the Czech Republic, Ireland and Germany. As a member of the "Wassenan Arrangement", Polish firms may not export to prohibited countries.

The defense industry continues to search for new export markets, particularly in developing countries and in the Middle East. Polish defense companies seek cooperation agreements or joint venture opportunities with foreign defense companies because the relatively lower cost of production in Poland (particularly for tanks, armored vehicles, artillery, ships, aircraft, and helicopters) will be attractive to potential customers. They believe that only such arrangements will permit them to survive through the current transition.

II. U.S. MARKET POSITION AND SHARE

In 1998, Poland was the only invitee country to sign the Central European Defense Loan (CEDL) agreement a USD 100 million program with the U.S. CEDL funds that can only be spent through the Foreign Military Sales program opened up more opportunities for U.S. companies. Through fiscal year 1999-2000, the United States has provided approximately USD 135 million in Foreign Military Financing (FMF) program grants, the majority of which are directly committed to programs and services in support of Poland's NATO force goals and minimum military requirements. This funding has been allocated to projects in air space management, command and control, search and rescue operations, communications equipment, mapping, meteorology, acquisition training, computers and more.

The NATO Security Investment Program (NATO-SIP) was established to help finance the military infrastructure development and modernization projects of its members. NATO-SIP will make USD 650 million available to Poland. About USD 380 million of the NATO-SIP funds are to be allocated to the modernization and renovation of seven military airfields, five fuel and material depots and two navy bases. About USD 10 million are earmarked for the development of Poland's military telecommunications system. The NATO-SIP funds have been made available up to the year 2006.

NATO investments in Poland in 2000-2006 include:

a) Telecommunication and Information Technology – USD 10 million – development of military telecommunication system for transmitting data and information between the Ministry of Interior, The Ministry of Defense, the General Staff, and the appropriate NATO agencies.

b) Polish Air and Defense Force – USD 280 million – to integrate the Polish Air and Defense Force along NATO standards. Projects include the opening of 6 radar centers and financing the purchase of 3 advanced technology radar systems (the remaining 3 systems will be financed by the Polish government). Another project is the final integration of the Polish Air Traffic Command and Control (ASOC) management system with NATO Integrated Air Defense Systems (NATINADS).

c) Infrastructure for NATO response forces operating on Polish territory – USD 360 million – modernization and expansion of 7 military airfields, 5 fuel, material and equipment depots, and 2 navy ports in Swinoujscie and Gdynia.

On October 10, 2000 three consulting firms were chosen by competitive bidding to provide modernization plans. Airports modernization was awarded to American company, NATO Expansion Engineering & Program Management Corporation, while modernization of fuel depots went to German firm Weidleplan Consulting, and modernization of navy ports to a Polish-Turkish consortium of Mostostal-Warszawa and Unitek.

For more information regarding NATO tenders contact the following:

Ministerstwo Obrony Narodowej
(Ministry of Defense)
Departament Infrastruktury MON
(Infrastructure Department)
Al. Niepodleglosci 218
00-909 Warszawa
tel: (48-22) 687-59-57
fax: (48-22) 687-43-29
Contact: Col. Zygmunt Bugowski, Chief NATO Cooperation Section

Ministerstwo Gospodarki
(Ministry of Economy)
Departament Rezerw Panstwowych i Spraw Obronnych
(Defense Department)
Pl. Trzech Krzyzy 5
00-904 Warszawa
tel: (48-22) 621—82-43
fax: (48-22) 621-88-24
Contact: Col. Witold Misiowiec, Director and Col. Tadeusz Kuzma, Deputy Director

C. END-USER ANALYSIS

Modernization Plans/NATO force goals

In response to slower-than-expected economic growth and strains on the MOD budget stemming from Poland's decision to accept 129 of a proposed 180 NATO force goals, the MOD modified its 15-year plan to a 6-year plan. This recently approved strategy attempts to link projected financial needs to military restructuring, and is Poland's first such comprehensive planning document.

Poland's military numbers have decreased from 450,000 in 1989 to 205,000. By 2002, Poland plans to reduce its forces to 150,000. Poland's military is traditionally land force heavy. Two thirds of the force is army, 23% is air force, and 7% is navy. Poland's military is undergoing sweeping changes - all designed to help it restructure itself into a more capable and mobile force compatible with NATO. The Polish Land Forces, after restructuring and downsizing is complete, will have six divisions, down from 11 divisions today. The Polish Air Force is grappling with rapidly aging Soviet-era aircraft. The Polish Navy has mainly coastal, minesweeping and ASW capabilities, although the acquisition by grant transfer of the U.S. frigate "Clarke" will provide a blue water capability.

Poland's military is essentially changing everything at once: force structure, staff organizations, training programs, doctrine, security procedures, etc. This makes for a very dynamic, as well as unsettling, situation for its officers. The changes in Poland's military and the reorganization/privatization plan for the defense industry must compete with other reforms. The state budget must also finance reforms in public administration, the education system, health care services and the pension system.

The Polish Defense Minister has stated near term spending priorities (in line with NATO force goals) as modernization of communication systems, building a new command and control network, the creation of an airspace control system and the integration of Polish air defense management with the NATO structure. The Prime Minister oversees an inter-ministerial committee charged with selecting a multi-role fighter and an attack helicopter for the army. The Minister of Economy and the Deputy Minister of Defense head this committee. An announcement (RFP) concerning multi-role aircraft, transport aircraft is expected in summer 2001.

The Government of Poland has identified full and active participation in NATO as one of its top foreign policy goals. NATO force goal requirements are driving equipment-related decisions, ranging from aircraft and helicopter to air navigation and communications equipment, to tank turrets and computers, to name just a few. Opportunities do exist for U.S. firms.

D. MARKET ACCESS

I. DEFENSE PROCUREMENT PROCESS

The survival of Polish defense industry firms is a driving factor in most procurement decisions. The Law on Offsets approved in 1999 mandates 100% offsets for all acquisitions over 10 million ECU in value. Polish companies need foreign partners to supply an infusion of capital and technology. The GOP favors purchases which entail such agreements. Foreign equipment sales in Poland frequently include co-production or joint venture agreements.

All tenders for amounts above 10,000 ECU must be officially announced. Tenders for lower amounts can be announced locally, in the local press or through local media. The law provides that tenders of very high value should be published in the Journal of European Economic Community. However, until Poland becomes a full member of European Union, this is not a requirement. The Bulletin of Public Procurement (Biuletyn Zomowien Publicznych), which lists public procurement opportunities throughout Poland, is now published twice a week. Subscriptions are available through:

Wydzial Wydawnictw i Poligrafii
Gospodarstwa Pomocniczego Kancelarii Prezesa
Rady Ministrow
ul. Powsinska 69/71
09-903 Warsaw

The following is a list of useful contacts regarding the procurement process:

Ministry of Defense
u1. Klonowa 1
00-950 Warszawa
tel:(48-22) 621-99-15
fax:(48-22) 845-53-78
Minister Bronislaw Komorowki

Ministry of Defense
Armaments and Infrastructure
A1. Niepodleglosci 218
00-911 Warszawa
tel:(48-22) 825-13-75
fax:(48-22) 825-21-52
Deputy Minister Romuald Szeremietiew

Ministry of Defense
Defense Policy Department
A1. Niepodlelglosci 218
00-911 Warszawa
tel:(48-22) 687-66-07
fax:(48-22) 825-28-22
Acting Director Colonel Ryszard Jeruzelski

Ministry of Defense
Military Equipment and Armaments
Al. Niepodleglosci 218
00-911 Warszawa
tel:(48-22) 845-01-53 or 684-41-77
fax:(48-22) 628-92-69
Director Colonel Janusz Zwolinski

II. IMPORT CLIMATE

Poland complies with the Harmonized Tariff System. Tariff rates are subject to change annually (in January). Depending on the country of origin, products are divided into three categories: developing nations, members of the World Trade Organization, and countries with which Poland has a bilateral or multilateral customs agreement (e.g., free trade agreements, CEFTA). In 1992, Poland signed an Association Agreement with the European Union (EU) that lowered or eliminated tariffs on many EU produced goods imported into Poland. Tariffs on U.S. products did not change. At that time, the U.S. managed to negotiate more favorable rates for some product categories, but many U.S.

products are still at a tariff disadvantage compared to EU competitors.

Customs duties apply to all products imported into Poland. Tariffs range from 0 (zero) to 45%, with the average between 15-20%. The customs duty code that is currently binding in Poland has different rates for the same commodities depending on their point of export.

a) EU Association agreement

In 1992 Poland signed an association agreement with the European Union that lowered or eliminated tariffs on many EU produced goods imported into Poland, while tariffs on U.S. products remained the same. At that time, the U.S. managed to negotiate more favorable rates for some product categories, but many U.S. products are still at a disadvantage compared to European competitors.

The most recent revision of the Polish customs tariffs took place on January 1, 1998. The average rate of duty in this new customs tariff is 7.73% for industrial products and 19.52% for agricultural and food products. The recent revision allowed Poland to adjust its foreign trade regulations to World Trade Organization and EU standards.

For some luxury and strategic products (e.g. alcohol, cosmetics, cigarettes, sugar confectionery, video cameras, satellite antennas, passenger cars, gasoline, and oil) excise tax is also applied. Excise tax is levied on top of the customs tariff.

As in much of Europe, a Value Added Tax (VAT) is also assessed. There are three VAT rates: 0%, 7%, and 22% depending on the product. VAT is levied on the CIF value of the product plus duty plus excise tax (if applicable).

Duty free quotas, or zero duty quotas, have been applied within certain industries including the automotive, computer, and pharmaceutical sectors in Poland. U.S. and foreign firms have benefited from these quotas. In some instances the quotas are targeted to products originating from specific export regions (e.g. cars from the European Union), and in others they have been assessed to help protect local industry (e.g. pharmaceutical), to help develop industries (e.g. computer parts and components), or to protect the environment.

Refunds are possible for customs duty paid on raw materials, semi-finished goods, and products used in the manufacture of goods for export within thirty days, contingent on documentation certifying customs duty was paid on the goods when they were imported.

b) Export/import issues

U.S. export license is required on shipments of certain commodities to Poland, as provided under the U.S. Bureau of Export Administration’s Commodity Control List. The government of Poland has established its own export control regime. Import documentation in Poland is compiled under a "Single Administrative Document" (SAD), and includes a customs declaration and certificate of origin. The SAD asks 56 questions about the goods, importer, place of origin, and method of payment. A completed customs value declaration is attached to the SAD. An original invoice or pro forma invoice proving the value of the goods is also required.

In general, the trade of goods and services is not restricted in Poland. In some areas, including imports of strategic goods (e.g., police and military products, radioactive elements, weapons, transportation equipment, and chemicals) a license or concession is required. The Ministry of

Economy issues import permits and concessions and regulates quotas. However, other Polish ministries have special jurisdiction over products such as tobacco (Ministry of Agriculture); permits related to air, sea, or road transport (Ministry of Transportation); industrial goods (Ministry of Industry); or natural resources (Ministry of Environmental Protection). The list of products requiring import certification in Poland is always subject to change, and appears to be growing. U.S. exporters should ascertain whether their product requires import certification before shipping.

In most cases, before an issuing ministry grants import permission on a product, the product must be reviewed and recommended for import into Poland by one or more inspectorates or technical associations, depending on the nature of the product. This can be a costly, lengthy, and confusing process for the U.S. exporter and the Polish importer alike. It is often necessary to submit samples of products or equipment for testing, regardless of the issuance of previous U.S. or international certificates. The presentation of detailed documentation on a product is a must, and all requests by relevant inspection agencies should be strictly adhered to in order to speed-up certification procedures.

When satisfied, the inspecting agency will make a positive or negative recommendation for import to the appropriate Polish ministry. Once import is approved for a specific product, further imports of that product are free from additional regulation. U.S. companies with several lines of similar products (e.g. pharmaceutical, food preparation, or chemical products) should begin the approval procedure on all products they anticipate they will export to Poland as early as possible.

Some products, once imported, also require registration. This is particularly true of products that come into contact with, or can affect the health of the consumer. In the case of hazardous materials, the importer must receive permission to use the product before applying for a concession to import the product into Poland.

III. TRADE FAIRS

Participation in a specialized fair proves to be effective way of promotion.

The major fair in defense sector is MSPO – International Defense Industry Exhibition. It is held each year in September, in Kielce. The nearest fair will take place on September 3-6, 2001. The organizer is:

Swietokrzyska Agencja Rozwoju
(Swietokrzyska Agency for Regional Development)
in cooperation with
Polska Izba Producentow na Rzecz Obronnosci Kraju
(Polish Chamber of National Defense Manufacturers)
ul. Warszawska 44
25-531 Kielce, Poland
tel:(48-41) 344-33-16 or 344-34-13
fax:(48-41) 344-32-09 or 344-63-45
e-mail: targisarr@bptnet.pl
Web site: www.narada.org.pl/arr/sarr
Contact: Ms. Malgorzata Mlynarczyk, Exhibition Manager (foreign exhibitors)
Tel:(48-41) 344-32-06

The other important exhibitions in this sector are:

International Air Show held in Radom. The nearest show will take place on September 7-9, 20001. The organizer of this show is:

Polish Air Defense Force Headquarters
ul. Zwirki i Wigury 103
00-912 Warszawa
tel:(48-22) 682-51-54
fax:(48-22) 682-55-29
e-mail: oniwzrw@wp.mil.pl

International Logistic Exhibition – logistic equipment and materials for armed forces, police, security, and custom service. The show is organized under the auspices of the Minister of National Defense and the Minister of Interior and Administration. The nearest exhibition will take place in Kielce on April 25-27, 2001. The organizer is:

Swietokrzyska Agencja Rozwoju
(Swietokrzyska Agency for Regional Development)
ul. Warszawska 44
25-531 Kielce, Poland
tel:(48-41) 344-33-16 or 344-34-13
fax:(48-41) 344-32-09 or 344-63-45
e-mail: targisarr@bptnet.pl
Web site: www.narada.org.pl/arr/sarr

IV. USEFUL CONTACTS:

For a complete list, U.S. companies should send an e-mail to Zofia.Sobiepanek@mail.doc.gov at the U.S. Commercial Service office in Warsaw. This information is provided only to U.S. companies.

For additional information please contact:
U.S. Commercial Service
American Embassy Warsaw, Poland

Mailing address (from the U.S.):
Department of State
5010 Warsaw Place
Department of State
Washington, DC 20521-5010

Street address:
U.S. Commercial Service
(IKEA Building)
Al. Jerozolimskie 56 C
00-803 Warsaw, Poland
tel: (48-22) 625-43-74
fax: (48-22) 621-63-27
e-mail: Warsaw.Office.Box@mail.doc.gov

Office of Defense Cooperation
Lt. Col. Peter Podbielski, Chief ODC
American Embassy Warsaw
Al. Ujazdowskie 29/31
00-540 Warsaw Tel: 011-48-22-628-30-41 Fax: 011-48-22-625-34-78